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June 20, 2005

VIA FACSIMILE NO. 521-3359 & POST

Robert F. Miller, Esq.
Dillingham Transportation Building
735 Bishop Street, PH 500
Honolulu, Hawaii 96813

Re: Claypool et al. vs. Isham; Civil No. 04-00570
Lexington Insurance Company Policy No. 1323464

Dear Mr. Miller:

You have inquired regarding whether Lexington will provide coverage or a defense to Blue Dolphin Charters, Ltd./Blue Dolphin Diving, Ltd. ("BDC") under the policy issued to Named Insured Eric Trout. While Lexington has never received a formal tender or a request for indemnity and a defense on that policy, and Eric Trout is not a defendant in any lawsuit nor has there been any allegations of wrongdoing by him, we will construe your questions as such a tender, and respond at this time. In that regard, please be advised that Lexington will continue to provide a defense to BDC in the above referenced litigation, under the policy issued to Eric Trout, subject to a reservation of rights, as explained, *infra*. Along those lines, Lexington will not withdraw the bond filed in the limitation action, but reserves the right to do so if coverage is determined not to exist.

Eric Trout is a named insured under Lexington policy no. 1323464 with effective dates of June 30, 2004 to June 30, 2005. Trout is a named insured pursuant to a certificate of insurance issued to him for an "occurrence" that is the result of any negligent acts, errors or omissions in the rendering or failure to render "professional services" as described in the declarations (SCUBA diving, snorkeling and swimming instruction and supervision and emergency first aid training). "Professional Services" is defined as "[t]hose services rendered by certified instructors, assistant instructors, dive masters, snorkel or swim instructors, dive control specialists (divecon)."

The Lexington policy provides additional insured coverage for BDC under Endorsement #001, however, such coverage is limited as follows:

EXHIBIT " F "

Robert F. Miller, Esq.
June 20, 2005
Page 2

1. The facility is only an additional insured with respect to liability arising out of the regular and usual operations of the Named Insured [Trout] in connection with the Named Insureds [Trout] teaching and/or supervising of SCUBA or snorkeling activities sanctioned and approved by PADI.

* * *

2. The insurance provided to such additional insureds does not apply to "bodily injury" or "property damage" arising out of a SCUBA diving training agency's providing or failing to provide:
 - a. training or educational standards or educational materials to any insured; or
 - b. supervision of SCUBA instructors, assistant instructors or dive masters.

Endorsement #003 also provides additional insured coverage for retail dive stores and dive boats from which an instructor, assistant instructor or dive master operates, but only for the regular operation of the named insured [Trout] in connection with his or her teaching or supervising of scuba or snorkeling activities sanctioned and approved by PADI. The endorsement, however, excludes coverage for the additional insured's rendering or failure to render "training or educational standards, or educational materials to any insured" or "supervision of scuba instructors, dive masters, or assistant instructors."

Based on the language of the above referenced endorsements, BDC only has coverage under the Lexington policy for claims arising out of a named insured's [Trout] teaching or supervising of scuba or snorkeling activities sanctioned and approved by PADI. Based on the current facts as known, it has not yet been established whether or not, on the day of the accident, Trout was teaching or supervising scuba or snorkeling activities sanctioned and approved by PADI. Furthermore, BDC will not be covered for its own conduct in providing or failing to provide to Trout or any other insured training or educational standards or materials or supervision of SCUBA instructors, assistant instructors or dive masters. Based on our understanding of the facts as developed thus far in the case, Trout appears to bear little if any exposure for the injuries involved in this case.

The purpose of this reservation of rights is to allow Lexington to review and/or investigate the claims asserted, and to respond to the claim without waiving any of Lexington's coverage defenses. Lexington reserves all rights pursuant to the terms, conditions, and exclusions of the policy, including, but not limited to, the right to deny any defense or indemnity obligation. Lexington specifically reserves the right to deny coverage for any judgment or settlement, to withdraw from the defense of BDC, and/or file a declaratory judgment action regarding Lexington's duties under the policy. Lexington further reserves the right to seek reimbursement for any amounts incurred in the settlement of any non-covered claims asserted against BDC, including attorneys' fees incurred by Lexington. Moreover, Lexington reserves the right to seek reimbursement for any amounts paid on BDC's behalf if it is later determined that the claims are

Robert F. Miller, Esq.
June 20, 2005
Page 3

not covered by the policy. Any information developed by Lexington in the course of its investigation may be used by Lexington to support its coverage defenses or to deny coverage.

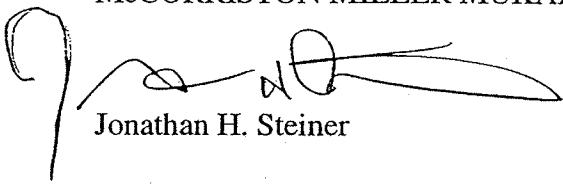
In addition to the coverage issues addressed in this letter, there may be other reasons why coverage does not apply, and Lexington does not waive its rights to contest or deny coverage for any other valid reason that may arise or is later discovered.

If you or BDC have any additional facts, material, or arguments which you believe bear on the availability of coverage, please provide us these materials so that we may fully consider them. Also, if any changes occur in the allegations in the claims asserted, or in the circumstances of this matter, please notify us immediately.

Thank you for your prompt attention to this matter.

Very truly yours,

McCORMISTON MILLER MUKAI MacKINNON LLP



Jonathan H. Steiner

JHS:jmc

cc: Evelyn J. Black, Esq.